Quarterly Market Report Mediterranean Region

Madrid Office

July - September 2003

Summary

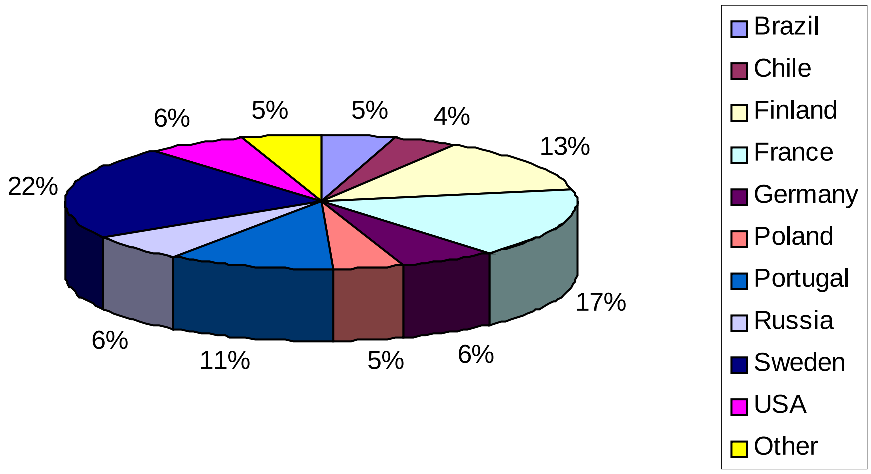
The recent developments of the import activities in Spain and Italy are reported here, together with an analysis of the long-term trend of U.S. softwood exports to Italy. Brief information about door production in Spain is included along with a notice about the moulding market and developments taking place, based on interviews with relevant molding manufacturers. The first section is completed with an overview of softwood production at a global level, based on published data by relevant trade organizations.

The second section is devoted to a number of activities completed during the period and the calendar of activities planned.

SECTION ONE

Trade Issues

Spanish Softwood Imports Jan.-June 2003

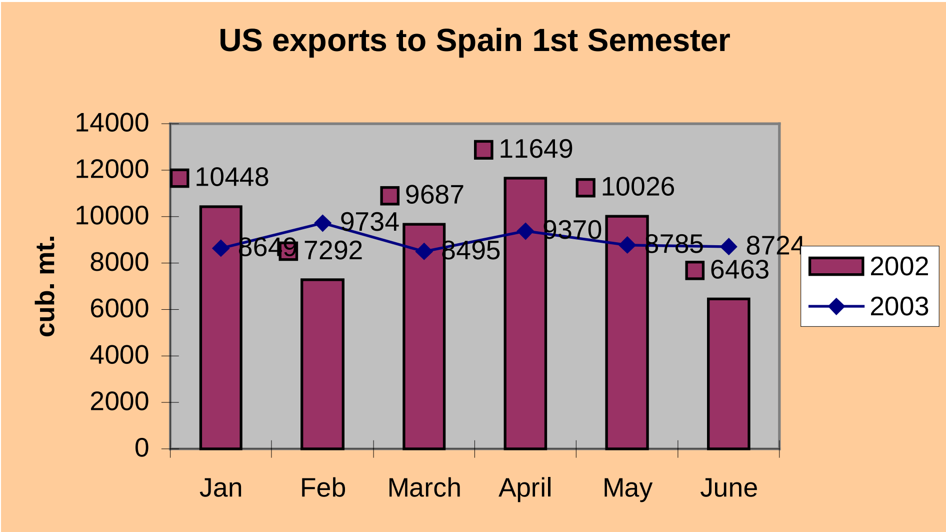


Solid-sawn softwood imports from Brazil, Poland and Chile experienced two- and even three-digit growth during the first half of 2003, but overall imports are basically stagnant. The severe drop in U.S. exports during the past two years seems to be restrained, comparing the situation to a year ago, with only a minimal decrease. Overall, the background situation shows a solid level of activity and it is expected that the second half of this year will see a recovery of the imports, particularly those traded in dollars.

Main Suppliers to the Spanish Wood Market (2003):

Country	2002 (Jan-June)	2003 (Jan-June)	%
Brazil	36,413	55,178	51
Chile	32,817	43,266	34
Finland	138,758	152,796	10,1
France	273,855	189,623	-30,7
Germany	60,858	69,802	14,7
Poland	17,831	51,475	188
Portugal	135,214	121,681	-10
Russia	49,239	71,509	45
Sweden	267,096	260,436	-2,5
USA	55,565	53,757	-3,1
All	1,143,667	1,126,173	-1,5

During the first half of 2003, no signs of recovery in the Spanish market exist, based on the lack of statistical data available at this time. With the exception of two months, provisional figures during 2003 of softwood imports in Spain from the U.S. show no improvement from the previous year. Currently, no sign of recovery exists for Southern Pine and other conifers, namely Douglas Fir. However, a stronger demand for cedar does exist. Some import volumes classified under pine probably correspond to other U.S. coniferous species, for which a North Eastern states origin could be assigned. Until now, though, no solid evidence has been obtained.



Source: Dir. Gral Aduanas

In the short term, the relief provided by the weakening of the dollar against the Euro is creating the right conditions for potential consumers of coniferous lumber to again focus their attention on American coniferous products. Unfortunately, the ground lost is probably already taken by other softwood species and a continued stability of the currency will be required to make the importers feel confident and able to resume higher volume purchases.

Interestingly, the relative volume of softwood lumber arrived under the harmonized tariff code 44071038, corresponding to dressed softwood lumber other than European spruce or pine, amounted to about 15% of Spain's total imports during the first eight months of 2003. Another observation is the relevant amount of imports (nearly 8,000 cubic meters) classified as European redwood, most likely a misclassification of the commonly imported Southern Pine. Part of the amount, however, could be Weymouth and/or Red Pine.

Production of Doors in Spain

Wooden doors are an important secondary product in the wood industry. In 2002 the production totaled more than 11 million units. This level of production is due to the demand in construction, with more than half a million dwellings built or remodeled.

In Spain, some 80% of the door production uses wood. The geographical situation of this industry is in both Castilias and Valencia, which captures 75% of the national production. The high-tech firms maintain a staff of more than 200 employees. The largest producers are manufacturing over one million units a year. This type of industry makes extensive use of particleboard as the core of the door, overlaid with veneer. Solid wood use is limited to the edges and moldings. Despite this small percentage of solid wood in the door unit, these large productions make use of sizeable amounts of Southern Pine, when used. An estimate of the approximate percentage of Southern Pine doors of this type is between 2% and 4% of current door production.

Despite the large portion of door production absorbed by the domestic market, manufacturers still pursue the export markets actively. In 2002, 10% of Spanish wood door exports (92 million Euros) reached this segment. The main destinations for this production are found in the European Union (Portugal, UK, France) but also in the U.S. and Mexico.

<u>Main destination of Spanish Wooden Doors in 2002/Euros</u>

1. Portugal -- 25,695,703.91
2. United Kingdom – 11,187,348.82
3. France – 9,093,365.91
4. USA – 4,784,448.87
5. Belgium – 4,084,585.49
6. Holland – 2,846,924.89
7. Marocco – 1,106,119.51
8. Germany – 502,967.05
9. Italy -- 466,946.05
10. Mexico – 67,207.89

First 10 destinations – 59,835,618.34
All countries -- 92,112,552.45

Southern Pine has been one of the preferred wood species in solid wood door manufacturing until recently. Other species are now favored, such as iroko, European redwood, and in some cases Red Cedar. This occurrence is caused by incorrect moisture content in the finished product resulting in checks, and excessive waste of raw lumber due to fast kiln drying. Other causes include a lack of proper finishing/preservative treatment, especially in exterior carpentry, and until recently an over-valued dollar. Furthermore, perception continues to point to high susceptibility to blue stain in Southern Pine. All of these concerns combined are pushing consumption of Southern Pine down and leading to increased market share of iroko, European pines and spruce, and other newcomers like larch and other tropical lumber.

Some of these causes can be attributed to the carpenter, normally lacking the necessary level of equipment or knowledge to counteract issues such as excessive moisture in the wood or improper finishing. But others are already built-in, like the check occurrence in the material caused by a forced kiln-drying process.

Checking in a dressed piece of Southern Pine.

The average carpenter making solid wood doors is a small/medium size company with little scientific background who relies on his own experience when making decisions about wood species and finishing. These carpenters are almost impervious to new or different ideas that may challenge their own experience, even if strong evidence is presented. The annual production of such workshops may be in the range of 10,000 to 30,000 units/year. They also provide the carpentry of the project typically, although they may be producing for the wood product dealers as well. In this case, it is a very price-sensitive market. During periods when the dollar was high, demand for Southern Pine diminished. Other market segments are less sensitive to price, but the specifier, typically the architect or the owner, has the final word.

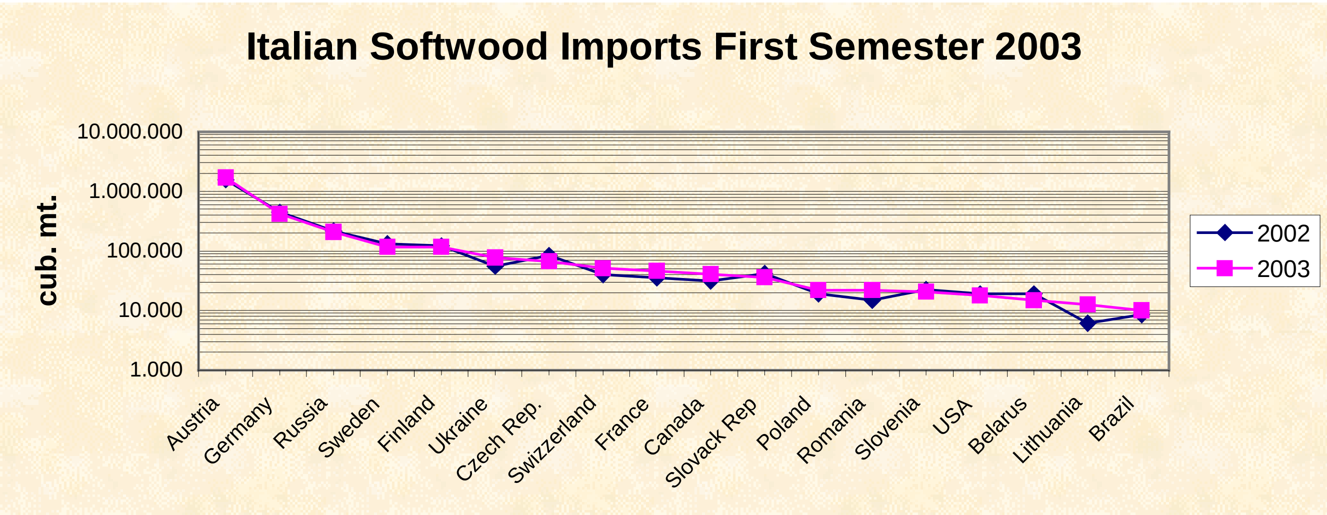
Mouldings

This most important market segment for Southern Pine remains relatively undisturbed after these years of difficulties for U.S. softwoods. The reasons for this prevalence are the unchallenged clear grades that only U.S. softwoods can offer on a consistent basis. However, potential threats remain in this application due to the following reasons:

- Advance of overlaid veneer/paper wrapped medium density fiberboard molding
- Competition from hardwoods: cherry, oak, maple, etc
- Little or no adaptation capacity of producers to customer-specific needs (i.e. sizes)
- Speed and flexibility of supply
- Preference for other woods of the architects
- Aesthetics
- Massive use of Southern Pine in the past
- Unavoidable presence of exporters
- Fewer companies producing clear grades (i.e. little competition)
- Too many intermediaries pushing the price upwards
- Suspicion of price fixing by exporters
- Frequent checks caused by forced kiln drying
- Deafness to claim settlement
- Susceptibility to blue stain

The Italian Market

The Italian market has not been especially active during the first half of 2003. Altogether, imports were below last year's volume but individual exporters have made progress in this market. The main supplier, Austria, could even increase volumes by 3% despite rather dull activity, while other competitors fared worse like Sweden and Finland. As for U.S. activity, the first half of the year has seen a slight decrease in volume, but does not necessarily indicate a trend towards additional reduction in export volumes. Most likely, the drop in U.S. exports to Italy is due to the major losses that have already taken place and because opportunities to expand are more viable during the months ahead than in the past two years.



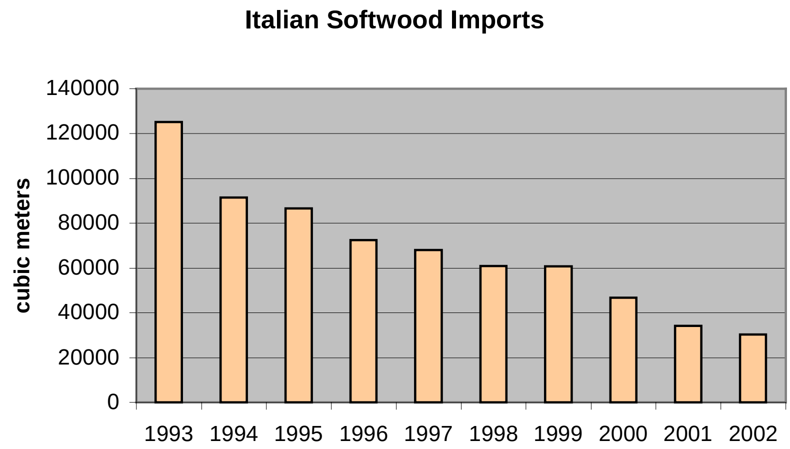
Main suppliers to Italy 2003

First Semester

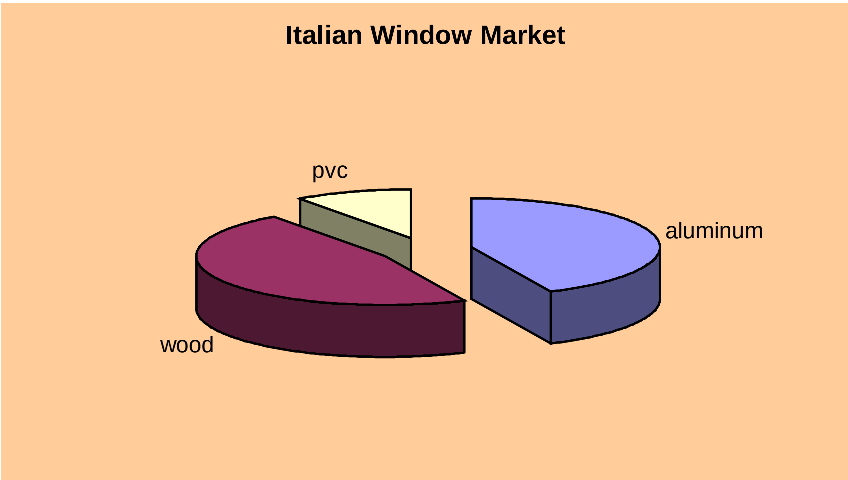
	2002	2003
Austria	1,570.490.00	1,688,570.00
Germany	449,665.00	419,222.00
Russia	217,847.00	209,321.00
Sweden	133,209.00	117,202.00
Finland	121,696.00	116.506.00
Ukraine	55,119.30	77,683.40
Czech Rep.	83,278.90	67,338.20
Switzerland	39,897.60	50,925.90
France	35,038.60	46,194.00
Canada	31,220.20	40,600.30
Slavic Rep	41,320.40	35,987.80
Poland	19,087.20	22,214.70
Romania	14,757.80	21,888.80
Slovenia	22,598.00	20,627.50
USA	19,102.60	17,843.70
Belaruss	19,091.60	14,835.60
Lithuania	6,119.25	12,587.50
Brazil	8,458.72	10,054.00

The Italian market is largely served from its nearest wood basket, Austria, followed by Germany. Other countries that contribute effectively with exports are several former members of the Eastern block, principally Russia, Ukraine and the Czech Republic. Significantly, Canada is also an important supplier of softwoods to the Italian market with a healthy increase in exports during the first semester of 2003. It is interesting to note the lesser importance of Sweden as a softwood supplier to Italy, compared with the situation in Spain, where Austria is an irrelevant source but Sweden its largest supplier of carpentry fiber

Looking at long-term imports of U.S. solid-sawn lumber into Italy, a gradual lost of market presence is realized through the past 10+ years. Although the speed of reduction is moderated in 2002, these statistics indicate that the Italian market has changed the preference for other wood species. When comparing U.S. exports against the window market, it is clear that substitution took place.



Source: Instat

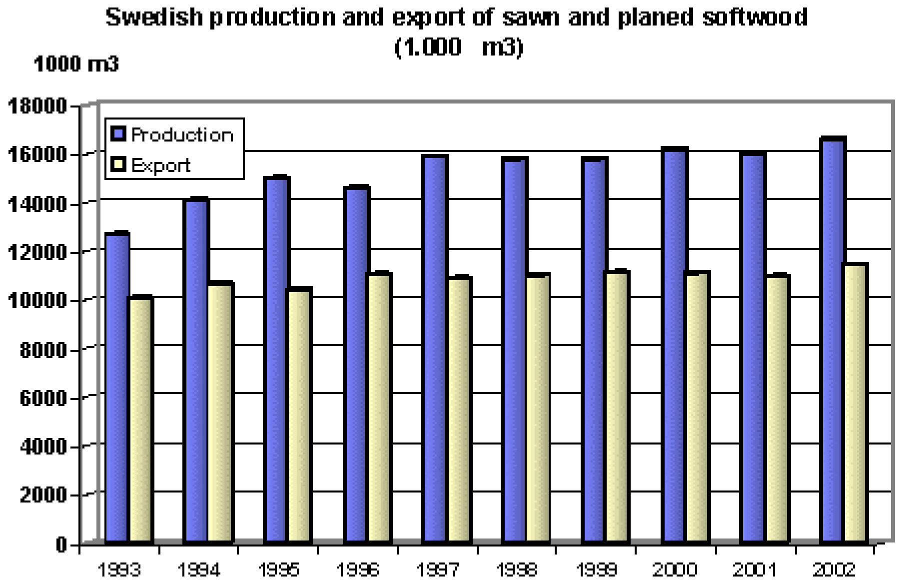


Source: UNCSAAL

The main market for U.S. softwood clears in Italy is window manufacturing. The percentage of wood windows in total production is nearly 50% of approximately 7.25 million units (1.69 sq.mt basis). This production has been reasonably stable during 1999/2002. The conclusion would be that other suppliers have taken a larger share of this market at the expense of American softwoods, traditionally Douglas Fir. Alternative woods like hemlock, cedar and Southern Pine introduced as a replacement to the former did reach only partial success. For the most part, laminated tropical and temperate hardwoods have captured the ground lost and also the slight growth of the total market.

The European Scenario for Softwood Lumber

The competition for market share in Europe is vital for several forestry dominated countries, like Sweden and Finland. The graphics below indicate the necessity for them to export the majority of its softwood lumber production.



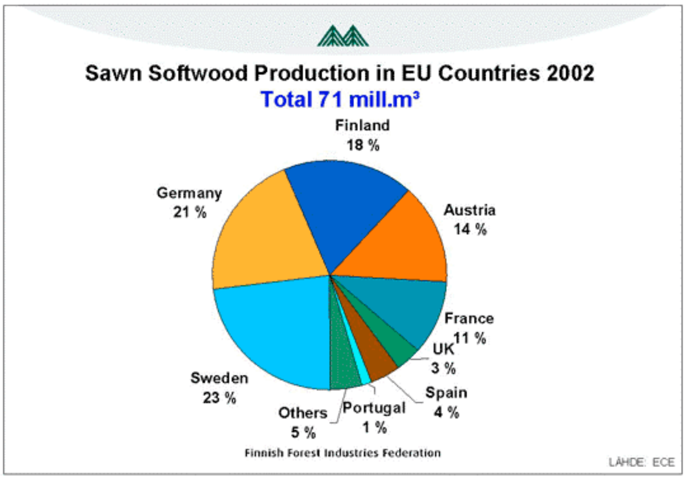
Of the total production (16,600 M m3), 69% was exported in 2002 and 76% of that volume (11,454) was shipped to European destinations. This includes sawn and planed products. The most important markets were the UK, Denmark and Germany. The Mediterranean countries (i.e., Portugal, Spain, Italy and Greece) purchased an estimated 10%, or slightly over one million cubic meters, of timber products from Sweden alone.

Other new players from the East have started also to seek a place in Western Europe, based on attractive prices and flexible production. The upcoming integration of the Baltic states and Poland in the EU will provide easier access to the Western and Southern European markets at prices difficult to beat.

As shown below, the four largest producers are active exporters as well with a healthy market share in either the Italian and/or Spanish markets. In addition, three of them are historically producing far more than they can absorb. Primarily Austria, and secondly Finland, are the leading suppliers to the Italian market, but Sweden and recently Finland have become two of the most important suppliers of sawn lumber in Spain. Neighboring France and Portugal are also major producers of softwood lumber and are increasingly shipping material to Spain.

As a result, forecasts point to an increase in tough competition in the future. In addition, new developments in the industry like thermal wood (treated with high temperatures to avoid using chemicals for extending the durability of coniferous species) by a Finnish company have created conditions for a long-term change in the lumber market. Other developments contributing include enhanced marketing efforts and direct trading with end users by small and medium size sawmills and exporters, together with a proactive approach to purchases by a number of carpenters (purchases of logs abroad, for example). United States exporters should carefully consider these changes if there is any interest in maintaining or retrieving part of the ground lost recently.

A more comprehensive picture on the sawn lumber production in Europe is shown in the graphic below.



SECTION TWO

Activities

Reverse Trade Mission

Organized by the Softwood Export Council, a group of Spanish importers participated in a trade mission to the U.S. West coast. The goal was to provide first-hand information about today's range of forest products. A number of visits were made to exporting mills, including secondary manufactured items and certified operations. The group was shown several species not traded in the Spanish market, which could easily be introduced. Examples include timbers like Ponderosa and Sugar Pine. The questionnaires returned indicated that this activity may produce actual short-term sales.

Trade Servicing

Following calls made to several importers and wood processors, the group visited Maderas del Noroeste to determine the level of importance that U.S. softwoods may have at the local level. As a result, the group learned that coniferous lumber in the region of Galicia is not one of the most demanded options. However, a modest demand for Red Cedar was confirmed from this company.

A molding manufacturer that was visited announced the company's research to improve the fire resistance of their moldings. From the wood species tested, the findings show that for the new product line only European redwood and Southern Pine absorbed the treatment to the levels required. The new product will be in the market within a few months.

Another molding manufacturer reported the shrinking volumes of Southern Pine usage due mainly to changes in fashion and its massive use in the past. Several door manufacturers confirmed this trend, and added that the excessive waste of wood caused by internal checks is leading them to continuously look for alternatives. In other parts of this report, attention is given to door makers buying logs abroad for their own needs. However, the relaxing of the U.S. dollar may increase the demand, according to several sources.

Advertising Campaign

An advertising campaign was held July through September of 2003, covering several of the main titles of the timber trades and the distribution. Although it is too early to draw conclusions, the number of responses received after the insertion of the ads indicate that the impact has been moderate. A public relations plan was launched along with the ads. By the end of September more than 40 pieces were published.

Calendar of Activities

October 15-18 -- Eurowindoor meeting, Athens, Greece.
November 6 -- Seminar, Menorca
November 12-15 – Maderalia trade show, Valencia, Spain.